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No. 614

In the Supreme Court of the United States

OCTOBER TERM, 1940

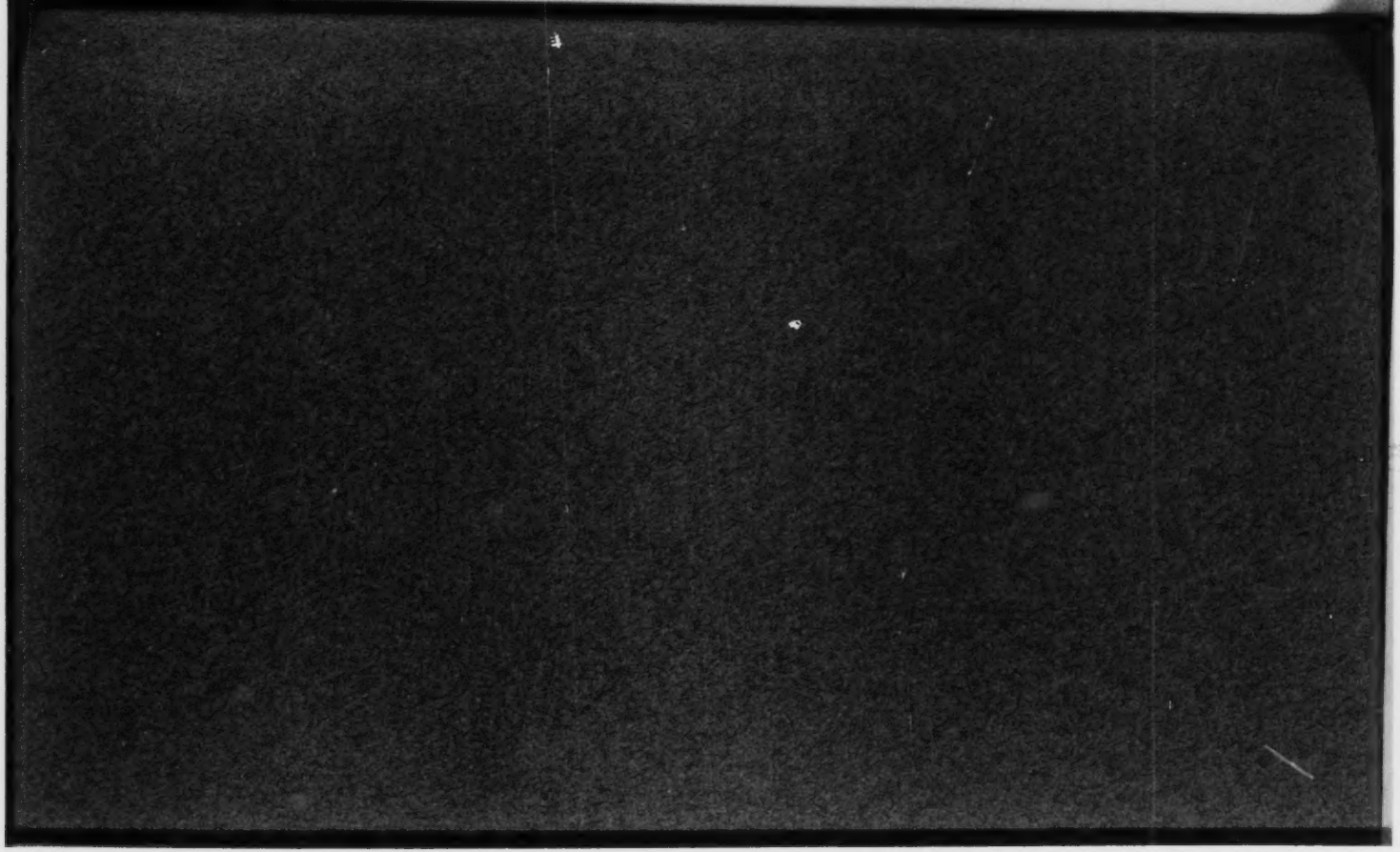
VALLEY WASTE MILLS, PETITIONER

v.

W. E. PAGE, JR., AND FIRST NATIONAL BANK OF ATLANTA, EXECUTORS OF THE ESTATE OF W. E. PAGE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENTS IN OPPOSITION



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OPINION BELOW

The District Court's findings of fact (R. 20) and conclusions of law (R. 27) are not officially reported. The opinion of the Circuit Court of Appeals (R. 30) is not yet reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered November 7, 1940 (R. 35). The petition for a writ of certiorari was filed December 10, 1940. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

A corporation during the taxable year disposed of cotton contracts calling for the future delivery of cotton during that year and was credited on the books of its brokers with the profits resulting from such dispositions. Simultaneously, it acquired contracts calling for later future delivery of the same quantity of cotton. The question is whether the profits credited to the taxpayer constitute realized gain for income tax purposes?

STATUTE INVOLVED

The pertinent provisions of the statute involved are set forth in the Appendix, *infra*, pp. 10–12.

STATEMENT

The relevant facts, as stipulated (R. 13–20) and as found by the District Court (R. 20–27), may be summarized as follows:

The taxpayer, a Georgia corporation, after filing with the Commissioner its claim for refund, which was denied, brought this suit to recover income taxes and interest alleged to have been illegally collected by W. E. Page, then a Collector of Internal Revenue (R. 21). The respondents are executors of Page's estate (R. 21).

On January 1, 1933, taxpayer owned contracts on the New York and New Orleans Cotton Exchanges calling for the future delivery of 10,500 bales of cotton (R. 21). All contracts on those cotton exchanges covering cotton purchased for

future delivery provide for delivery in less than twelve months from the date of purchase (R. 22).

The board of directors of taxpayer, prior to January 1, 1933, ordered that taxpayer's long or buyer's position be maintained in the cotton market to the extent of the quantity of cotton represented in the contracts owned January 1, 1933 (R. 22). The only way under the rules of the New York and New Orleans Cotton Exchanges in which taxpayer as owner of the cotton contracts could uninterruptedly maintain its long position over a period of time was to sell the cotton contracts calling for future delivery prior to the delivery date thereof and, simultaneously with the sale, buy cotton contracts calling for the future delivery of a like amount of cotton in a subsequent month (R. 22).

The taxpayer did maintain its long position in the cotton market by selling the cotton contracts prior to their delivery date and, simultaneously, buying new contracts calling for the same amount of cotton to be delivered in the future (R. 22). The profit or loss resulting from each sale, together with the expenses attending the sale, and simultaneous purchases, were reflected on the books of the cotton brokers through whom taxpayer traded (R. 22). The books of the taxpayer for the year 1933 also reflected such profit or loss resulting from the sale of each contract (R. 23). Whether all or any part of the credit balance could be withdrawn would depend on whether and to what extent it was

needed to meet margin requirements for the account (R. 22). No part of taxpayer's long position in cotton was liquidated until subsequent to the year 1933, and then by order of its board of directors (R. 22–23).

The Treasury Department, in computing the tax liability of taxpayer for the year 1933, ruled that each time a contract for the delivery of cotton in a particular month was sold, such sale constituted a closed transaction, and taxable gain or deductible loss resulted therefrom, despite the fact that simultaneously with such sale taxpayer purchased a cotton contract calling for the future delivery of the same quantity of cotton just sold (R. 22–23). It thereupon added to taxpayer's taxable income for that year the amount by which the gains exceeded the losses from the sales of the contracts (R. 23).

Taxpayer has been engaged in buying and selling cotton waste or re-worked cotton. In the year 1933 the board of directors of taxpayer ordered that active business of taxpayer be discontinued, except to fulfill contracts which had been made and to dispose of the inventories on hand; and further, that contracts for future deliveries of cotton be purchased to cover the amounts of waste so sold, and that its buyer's position so established by the purchases of such cotton futures contracts be maintained in addition to its buyer's position established by its prior purchases of cotton futures contracts. Pursuant to this action, as waste was sold, con-

tracts for the future delivery of 2,100 bales of cotton were purchased in the year 1933, and the extent of its buyer's position established by such purchases was maintained in the manner stated (R. 23).

It was stipulated orally at the trial that "With respect to each lot of cotton carried under the transactions involved, the plaintiff finally closed out the lot (treating the switching from one month's delivery to a later delivery as not a closing out) at a net loss on the transaction" (R. 24).

The District Court concluded (R. 28) that under the taxing Act each sale in this case was a closed transaction, and that the taxpayer was not entitled to recover. The Circuit Court of Appeals affirmed (R. 30–35).

ARGUMENT

The sales of cotton contracts at more than cost gave taxpayer a credit balance on its brokers' books subject to its immediate withdrawal except to the extent needed to meet margin requirements (R. 22). There is no evidence showing what the margin requirements, if any, were at various times and, so far as is known, taxpayer may have withdrawn its profits in whole or in part in the form of cash. The sole question is whether the profits thus subject to the control of taxpayer may be included in its taxable income. The only reason advanced for exempting these profits from taxation is that taxpayer, pursuant to a predetermined plan,

simultaneously purchased other contracts calling for a like amount of cotton. It is urged that there was no change in taxpayer's economic position and therefore no *realization* of gain (Pet. 4, 5–7).[1] Neither the premise nor the conclusion of the argument is sound.

1. As a matter of fact there was a very decided change in taxpayer's economic position—one in no way comparable to a mere postponement of the delivery date of the contracts. The taxpayer in the case at bar started with a contract for cotton deliverable at a certain date and ended with a contract for cotton deliverable at a different date, together with cash or its equivalent. It may, so far as the record shows, have taken that cash and spent it. One who merely postponed the delivery date of the contracts would not *realize* upon any increase in their economic worth and, of course, would not receive cash or its equivalent during the taxable year as taxpayer did in this case.

2. The closest analogies fully support the decision below taxing these profits. It is settled that a gain may be "realized" by a taxpayer upon a mere change in the nature of the legal rights held though there has been no addition to his economic worth. *Helvering* v. *Midland Ins. Co.*, 300 U. S. 216, 225, and cases cited. Here there was not only an increase in the economic worth of the contracts

[1] No contention is made that the gain, if *realized*, should not be *recognized* under Section 112 of the Act.

but the increase was made available to taxpayer in the form of cash.

Whether taxpayer chose to enjoy its profits, as it may have done, or to leave them with its broker as margin for other commitments, in either case the profits are equally subject to the income tax. *Webb* v. *Commissioner,* 67 F. (2d) 859 (C. C. A. 2d); *Baker* v. *Commissioner,* 81 F. (2d) 741 (C. C. A. 3d); *Foley* v. *Commissioner,* 94 F. (2d) 958, 962–963 (C. C. A. 3d), certiorari denied, 305 U. S. 615; *Sachs* v. *Commissioner,* 111 F. (2d) 648 (C. C. A. 6th); *Burrows* v. *Commissioner,* 38 B. T. A. 236. Compare *Corliss* v. *Bowers,* 281 U. S. 376. And the fact that in a later year the taxpayer may have closed out its holdings at a loss greater in extent than its profits during the year in question is wholly without significance. Such a result is a frequent and inescapable consequence of laying income taxes upon a taxpayer's operations during a twelve month statutory accounting period. *Burnet* v. *Sanford & Brooks Co.,* 282 U. S. 359, 364. We submit that there is no merit to the taxpayer's contentions.

3. The taxpayer cites no case concerning cotton futures contracts or trading in marginal accounts. It is believed that, despite the asserted frequency of such transactions (Pet. 5–6), there are no decisions supporting taxpayer's position.

Various cases are cited (Pet. 6) for the proposition that in tax matters substance and not form

should prevail. There is a short answer to the contention based upon those decisions. The substance of the transactions in question is that taxpayer's cotton contracts, which had increased in value, were sold in a manner permitting the increase to be received by taxpayer in cash or its equivalent.

The remaining cases cited (Pet. 7) involve claimed deductions for losses on the sales of stock where efforts were made to circumvent the wash-sale provisions of the revenue acts or where the taxpayer retained an interest in or control over the property in form sold. The issue in those cases was whether the taxpayer could take a deduction for a loss where it had not definitively disposed of the property. Here, quite a distinct issue arises—whether an admitted profit which was reduced to cash during the taxable year is subject to income tax in the hands of taxpayer. Compare *Burnet* v. *Commonwealth Imp. Co.,* 287 U. S. 415, with *Higgins* v. *Smith,* 308 U. S. 473.

CONCLUSION

The judgment of the court below is plainly correct. There is no conflict of decisions, and no question of general importance is presented. The petition for a writ of certiorari should therefore be denied.

Respectfully submitted.

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